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March 8, 2010

Ms. Mary Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

Subject:Comments on Part 704 Corporate Credit Unions

Dear Ms. Rupp:

On behalf of America's Christian Credit Union, I appreciate the opportunity to comment on NCUA's proposed amendments to Part 704, which would make major revisions regarding corporate credit union capital, investments, asset-liability management, governance, and credit union service organization (CUSO) activities. I recognize that the NCUA Board and staff have spent an enormous amount of time, effort, and consideration in researching, discussing, soliciting and evaluating input, and creating the Advanced Notice of Proposed Rulemaking and this proposed rule. NCUA's desire to improve and strengthen the corporate system is evident in the scope and breadth of this proposal.

Before I go into specifics as it relates to the proposed changes in this regulation, I believe it's prudent to provide the NCUA Board some context of my history and perspective that brings me to the statements and opinions that are contained herein. I have been in the credit union movement for 33 years, and have been President/CEO of America's Christian Credit Union for 24 years. During that time, I had the distinct honor and privilege to serve on the Supervisory Committee of WesCorp, serve as Chairman of the Supervisory Committee of WesCorp, and serve on the Board of Directors of WesCorp. In addition to that, I have had the honor of serving on different secular and non-profit boards, some of which are financial in nature and others that have multiple missions.

As a result of my history within the credit union system, I can recall the days where our credit union and virtually all credit unions were forced to shop for credit lines and back office services from banks prior to when the corporate system was established. I distinctly recall the partnership that we shared with Security Pacific National Bank, and how quickly that came to an end when Bank of America acquired them. I can also recall that our quest to find financial services that are now afforded to us by WesCorp was often met by a resounding 'No,' from other banks, or a yes with extraordinary strings and conditions attached to their agreement to provide such basic services.

It strikes me as somewhat odd that very few of the principles at NCUA have this kind of important and valuable historical perspective that strikes at the heart of why a corporate system, and I trust, WesCorp, will be able to be sustained. It seems as though they are operating from a purely technical or theoretical viewpoint which I have great respect for, but I believe should be equally balanced with historical experiences that I and many of my colleagues who have been in the industry for 30+ years share, and should be taken into account in the reshaping of our corporate credit union system.

There has been a lot of talk about the aversion to systemic risk within the credit union system, and I for one, applaud that avoidance and certainly want to be a participant in curbing as much systemic risk that the credit union system has; however, I have seen more experiences than I care to share that **failure to have a credit union owned system will create an enormous systemic risk for individual credit unions and the credit union system.** I want to warn the NCUA Board and staff that if credit unions are forced, as a result of NCUA's quest to demolish the corporate system and force us to go out and acquire lending, investment, back office payment processing and check clearing services from other banks and financial institutions, this indeed in my opinion, create a more systemic risk to the system and the over 90 million credit union members nationwide than what we find ourselves in. My experience has borne out the fact that these other financial institutions do not share our credit union mission or philosophy and clearly do not have our interest at heart. With the merger and acquisition activity that is rampant among other financial institutions, relationships formed today can overnight be virtually wiped out and the credit union will either be left holding the bag for such vital and critical services as I've just described, or will be forced to make immediate changes that may not afford them the time to do the necessary due diligence to ensure that it's a sound, safe business transaction.

However, with that said, I regret to state that in our view, the proposal raises far more substantial concerns than it provides realistic solutions. **There are several provisions that, if enacted as proposed, will make it essentially impossible for corporate credit unions to operate in a viable fashion.** Further, many of these provisions will have harmful effects on natural person credit unions and, ultimately, their members.

While I provide many recommended modifications to the proposal in this comment letter, given the extensive shortcomings of the proposal, as well as what is at stake—the possible viability or non-viability of a credit union-owned corporate system—**our Board urges the NCUA to withdrawal the proposal as drafted so that a more cohesive and feasible set of rules can be crafted. We strongly believe that *there should be another round of proposed rule making for Part 704—with another 90 day comment period—before issuing final rules to govern corporate credit unions.***

704.8 – Asset and liability management
(c) Penalty for early withdrawals
The elimination of the ability for a corporate credit union to redeem one of its certificates at a premium puts the issuance of share certificates by corporate credit unions at a significant disadvantage, and **will likely destroy or make non-economical, the institutional funding market for term certificates.**

Corporate share certificates are a direct competitor to U. S. Agency issued debt. Corporates have been able to compete effectively by comparing the two investment alternatives. They pay a higher yield to investors and can be structured to exactly meet investor needs rather than take whatever the Agency market happens to be offering. In terms of collateral value, they may assign 100 cents on the dollar regardless of market value, whereas Agency debt is assigned a percentage of the prevailing market value. As far as liquidity goes, both can be "sold" at prevailing market prices.

The proposal limits a corporate credit union's ability to pay a market based redemption price to no more than par, thus eliminating the ability to pay a premium on early withdrawals.
By removing the comparable liquidity option, **all corporate certificates are at a distinct disadvantage that brokers will be very quick to point out to investors.**

Adopting this proposal will have the impact of **significantly reducing overall liquidity in the corporate credit union system as brokers of Agency securities stress that the yield pick-up is inadequate to cover the credit risk and the lack of liquidity.** Corporates will not be in a position to counter that argument by increasing the spread differential, because investment restrictions will make such issuance totally unprofitable.

Frankly, I do not see why our credit union is not able to obtain a premium on certificate redemption if we need liquidity. **If this proposed change stays in, we will have to seriously consider putting my longer-term investable funds elsewhere in liquid instruments that do not penalize early redemptions. All credit unions will be forced into the same choice, which will effectively mean the end of corporate certificates as a competitive investing option.**

This proposal appears to be a misguided attempt to insure system liquidity, and will have the opposite effect as well as prevent the emergence of a sound funding strategy for all corporates. We would strongly urge that this proposal be stricken from the final rule.

704.8 (d) – Interest rate sensitivity analysis
The rule on NEV shock testing to control interest rate risk has been in effect for those corporate credit unions that have expanded authorities and basically has proved to be a valuable control point for interest rate risk since its inception some 12 years ago. The 3 percent threshold does reduce the amount of analysis for those corporates that do not seek to take interest rate risk, whereas the old rule required monthly testing regardless of the results of the previous test.

704.8 (e) – Cash flow mismatch sensitivity analysis
This appears to be a knee jerk reaction to the recent events and the resulting freezing of the credit markets. It amounts to setting limits based upon a once-in-a-lifetime, totally unexpected event. The spread widening of 300 basis points coupled with a decline limited to 15 percent is too restrictive and will severely hamper a credit union from generating net interest income.

For fixed-rate institutions, this will increase the amount of risk assigned, as the same 300 bps decline will be discounted at a lower rate in the credit shock environment. This will add from 1% to 15% additional volatility to a fixed rate instrument depending on remaining tenor. For floating-rate instruments, the impact will be much more significant. The credit spread shock will apply to the entire life of the floating-rate instrument, effectively converting it to a fixed-rate for measurement purposes. This means that a 1-month floater with a 2-year maturity will have a risk profile of -0.25% in the +300 bps interest rate shock test but will be assigned a -5.97% in the credit spread shock test. Floating-rate instruments are normally attractive investments for a corporate as they react quickly to changes in interest rates giving relatively stable price profiles, but their attractiveness would be eliminated under this test. **This means that it is effectively mathematically impossible to have a -5% interest rate risk volatility and pass the -15% credit spread shock test.**

Our analyses indicate that **there is no combination of assets, with a 2-year average life and limited extension risk that could generate sufficient margins to attract funding *and* pass a 300 bps credit shock test.**

Also, section 2 clearly rules that derivatives are to be excluded from the shock test even though these are not immune from the impact of credit union spread widening. Additionally, the Part III (derivatives expanded authority) specifically allows credit derivatives, which are available to mitigate the very risk being tested! It is inconsistent to allow derivatives that hedge credit spread widening yet disallow those transactions from credit spread widening shock test.

Historic analysis indicates that 100 bps would be an unusual and rare event in the market sectors that would be allowed under the new regulation. Over the last 15 years, excluding recent events, Credit Card and Auto ABS credit spreads to LIBOR widened to a maximum of around 50 bps, and generated a standard deviation of spread volatility of around 10 bps.

It would seem more realistic to set the credit shock test at 100 bps widening – double the historical average. Even at 100 bps credit shock, a NEV volatility limit of 35% decline is needed to accommodate the impact of the floating-rate investments carrying the loss to maturity.

Additionally, there is a significant difference between Agency issued instruments and other non-government guaranteed securities. Debt of Government Sponsored Entities ("GSE") would not carry concentration limits in the proposed rules. These securities trade in very large and liquid markets. We recommend using a lower credit spread shock, for example 50% of the regular spread shock, for securities issued by GSE's.

If this proposal is left unchanged, it will have severe repercussions on the future viability of the corporate credit unions. Any ability to generate a reasonable interest margin to build retained earnings will become very dependent upon a lower cost of funds for the corporate. That means a lower yield paid to members.

We would urge NCUA, to amend this test to a more realistic test of a 100 bps credit spread widening and a 35% NEV volatility tolerance limit, and consider a reduced shock for GSE debt. The role of derivative transactions also needs to be consistent with other parts of the proposed rules.

704.8 (f) – Cash flow mismatch sensitivity analysis with 50 percent slowdown in prepayment speeds

Non-mortgage ABS (Auto, Credit Card, and Student Loan) historical prepayment speeds do change modestly from time to time, but prepayment changes are driven more by the prevailing economic conditions rather than interest rate or credit events. There is no factual or historic basis for halving ABS speeds in the context of a credit risk shock test. Floating-rate, non-mortgage ABS securities are a lower risk, reasonable return investment, of which **the corporates' ability to purchase would be severely constrained under this test when the proposed rule already applies concentration limits.**

MBS principal paydowns are subject to interest rates and prevailing economic conditions. The portfolio/asset limit of 2 years in weighted average life, along with the credit shock and pay-down slowdown tests will effectively make holdings in MBS (the single largest asset-backed sector) virtually impossible.

Non-mortgage ABS and Agency MBS are lower-risk securities, with a reasonable return, which the credit shock tests will largely exclude from corporate balance sheets under the proposed rules. **The**

return on investment these securities provide will be crucial if corporates are to meet proposed growth targets in Reserves and Undivided Earnings (RUDE).

If this proposal is left unchanged, it will again, have severe repercussions on the future viability of the corporate credit unions. The largest sector of potential investments – Agency and Private Label Mortgage Backed Securities – will be effectively closed to corporate balance sheets. **The ability to generate a reasonable interest margin will become very dependent upon a lower cost of funds for the corporate. That can only mean a lower yield paid to members.**

We would urge NCUA to abolish this test and rely on the periodic analyses provided for in Section 704.8 (d) 2 (ii) or amend this test to allow a 50% NEV volatility tolerance limit. Some consideration should also be given to scaling the credit shock to the weighted average life of GSE issued securities.

Bottom line is, the analyses show that the proposed limitations placed upon a corporate through various NEV tests do not allow the corporate to generate sufficient interest margin to build retained earnings to meet your proposed capital requirements. This is simply unacceptable! If enacted as a drafted, this proposal will inevitably lead to some combination of increased fees being charged to me and forced expense reductions that will adversely impact the level of service and support that my credit union needs. The rule should be revised to allow for **WesCorp to make sufficient income from the balance sheet** to grow and invest in innovation for the benefit of all its member credit unions, while exercising an acceptable level of credit and interest rate risk.

704.8 (h) – Weighted average asset life
This clause limits the term or weighted average life of a corporate credit union's investments. Furthermore, there are various implications for natural person credit unions from this section of the rule.

First, a corporate's ability to make term loans to natural person credit unions beyond two years will be adversely affected. Although not clear in the language of the rule itself, NCUA has stated that the investment portfolio *must* include loans to members and CUSOs. **A corporate wishing to make loans to natural person credit unions will have limited choices.** In order to keep the overall weighted average life of the portfolio within the two year limit, most of the loans made will be limited to shorter-term maturities. For longer-term loans a corporate credit union will have to increase the rate offered substantially in order to compensate for the impact the longer term will have on this WAL test.

In order to meet potential lending demand from members, a corporate will have to keep its securities portfolio well under the two-year limit, so as to not have a single loan cause a breach of the limit. The two-year limit is already a severe constriction on Net Interest Income generation. Including loans in the calculation will force a corporate to choose between enough income to survive and being in the term lending business with members.

If the proposed rule is adopted, longer-term financing available to natural person credit unions from corporate credit unions will be reduced drastically and what will be available will come with a much higher borrowing cost.

A second impact of this part of the proposed regulation is the effect it has on a corporate credit union's ability to earn an adequate yield on its investment portfolio. One way a corporate credit union adds yield to its portfolio is to move out the maturity spectrum. Securities with longer maturities or weighted average lives typically earn higher yields to compensate investors for the additional interest rate risk inherent in the longer term. Much of this interest rate risk can be mitigated through the use of derivatives within a prudent interest rate risk management program. The current NEV testing required of corporate credit unions adequately measures and limits this risk. This WAL restriction will lower the yield a corporate credit union will be able to earn on its portfolio and will lead to lower rates available to natural person credit unions on corporate credit union certificates.

A third effect from this part of the proposed regulation will be on the asset mix of a corporate credit union's investment portfolio. This weighted average life limit will make it very difficult for a corporate credit union to invest in agency mortgage-backed securities. As mentioned above, the interest rate risk inherent in mortgage-backed securities can be somewhat offset through the use of derivatives. One might argue that this WAL test gives a clearer picture of an institution's liquidity of its investment portfolio relative to its liabilities. However, agency MBS are highly liquid instruments that can be easily sold if liquidity is needed. Unlike non-agency MBS, agency pass-through securities have no credit risk and pose very little risk to a widening of credit spreads. There are very active and liquid markets for borrowing using agency MBS as collateral should liquidity needs arise.

Agency MBS, used properly, are a prudent investment alternative for corporate credit unions. **This restriction will preclude the use of such instruments and will reduce the yield potential on a corporate credit union's portfolio, thus lowering available rates on corporate credit union certificates.**

We would propose that **loans be excluded from the calculation of weighted average life of the investment portfolio.** Additionally, we recommend a longer restriction on weighted average life of 3 years and that Agency and government-guaranteed securities be treated separately with a longer weighted average life restriction of 5 years.

704.6 – Credit risk management
Federal funds transactions are used to invest short-term liquidity. This is particularly important given the inter-month cash variability a corporate credit union typically experiences.

Federal funds transactions are not specifically excluded from the sector concentration limits, so Section 704.6 (d) (3) takes effect limiting aggregate federal funds transactions to the lower of 100 percent of capital or 5 percent of assets. **This limit would severely limit a corporate's access to the federal funds market.**

Further, in paragraph (4) of Section 704.6 (d) allows for an exemption to the concentration limit rules for deposits in other depository institutions but not specifically for federal funds transactions. Although Fed Funds transactions are nearly identical in practice to large wholesale deposits, they are considered sales and are not included in this exemption.

Corporates will have difficulty investing ample short-term liquidity at reasonable rates. They may also have to reduce the rate they are paying to their member credit unions on their overnight accounts.

We would urge NCUA to change the definition of deposits to include Federal Funds or to change Section 704.6 (d) (4) to include Federal Funds transactions sold to other depository institutions in the exemption from concentration limits.

704.6 (c) – Issuer concentration limits
The limit on aggregate Federal Funds sales to a single obligor is 25% of capital. There are a limited amount of counterparts that are bidding for Federal Funds at any one time in the marketplace. This limit is too small given the limited amount of counterparts bidding and will cause difficulty in managing a corporate's short-term liquidity position.

Corporates may have difficulty investing short-term liquidity at reasonable rates. Again, they may have to reduce the rate they are paying to member credit unions on their overnight accounts.

We would urge NCUA to change Section 704.6 (c) to allow a larger single obligor limit of 2005 of capital on money market transactions with a term of 90-days or less. An alternative solution would be to specifically allow a single obligor limit of 200% of capital for Federal Funds transactions sold to other depository institutions.

Part III Expanded Authority – Derivatives
Credit risk on Derivatives used in the manner described in the current and proposed regulations is much less risky than investments. **Derivative contracts are not investments.** Yet the proposed regulation holds derivatives to the same standard as investments.

Master ISDA agreements are in place with each derivative counterpart, which allows for netting of exposures and requires collateralization of mark-to-market exposures beyond a predetermined threshold. This significantly limits the credit exposure on a derivative to the threshold amount, which is a small amount and in many cases near zero.

As I assume you are aware, derivatives are typically executed with major commercial or investment banks. By holding derivatives to the same standards as investments, corporates will be restricted to using counterparts that are rated AA- or better. Currently there is just one counterpart that has a rating of AA- or better. **The proposed regulation would severely restrict a corporate from executing derivatives due to a lack of counterparts.**

Corporates would lose the ability to execute derivatives, which would limit their ability to manage interest rate risk. It would also limit the corporates' ability to issue structure products such as floating, callable, step-up or amortizing certificates.

Credit unions would lose an attractive higher-yielding investment vehicle that would compete with Agency securities. Furthermore, corporates would not be able to provide a hedge program to member credit unions.

704.6 – Credit Risk Management (f) – Credit Ratings
The long-term liquidity options for credit unions would be diminished because corporates would have to limit the term loans they offer to members.

We would urge NCUA, to exclude derivatives from the investment credit ratings and concentration limits. Furthermore, I would suggest creating a separate limit of 5% of capital as the maximum exposure threshold amount allowed to be negotiated in the Master ISDA agreements with counterparts.

704.19 – Disclosure of executive and director compensation
This section requires that corporates provide to their members certain information about the compensation and benefits of senior executive officers and directors.

Section 704.2 defines a *senior management employee* as: [A] chief executive officer, any assistant chief executive officer (e.g., any assistant president, any vice president or any assistant treasurer/manager), and the chief financial officer (controller). This term also includes employees of any entity hired to perform functions described above.

In the currently proposed regulation, the definition of "senior management" is too encompassing and broad – far more than what is required of publicly-traded companies governed by the SEC.

Failure to make such a change could cause a corporate credit union to experience difficulty recruiting mid-level executive positions based on its inability to keep salary data confidential.

The definition of "Senior Management Employee" should be changed to include only the top wage earners of the corporate (similar to the SEC rule II.C.6.a). The definition would include the President and CEO, the principal financial officer and the three most highly compensated executive officers.

704.11 Corporate Credit Union Service Organizations (Corporate CUSOs)
Regarding (e)(3) ("Other categories of services as approve in writing by NCUA and published on NCUA's website") Permissible activities under Section 704.11 (e)(3), are completely nonexistent and undefined. Additionally, it is unclear which current Corporate CUSOs would be allowed.

Credit unions will lose a competitive advantage in the marketplace if Corporate CUSOs have limited ability to invest in and/or offer services that will enhance their abilities as financial institutions. Such ambiguity in the regulation will lead to credit unions looking outside the credit union systems for solutions that could and should be offered by Corporate CUSOs. **We would expect such gross ambiguities to be clearly defined in the final rule.**

Additional Concerns
We are certain that no credit unions will be willing to contribute additional capital in such a short time frame, and in such an uncertain environment. Indeed, some credit unions may decide to pull their deposits from the corporate system as the result of such a precipitous move to achieving a 4% Leverage Ratio via PCC. This, in turn, would lead to liquidity concerns for corporates. **We recommend that NCUA clarify its intention with respect to the time period for capital ratio attainment.** Given the unavoidable reality that credit unions will need longer than one year before they will feel comfortable recapitalizing corporates, **we urge NCUA to recognize that: (a) some kind of financing or capital note (equivalent to 4% of a corporate's balance sheet) will be required to meet corporates' operational needs; and (b) the proposal's time period for attaining the risk-based capital ratios must be extended to at least three years.**

We believe the proposed model violates principles of concentration risk, represents too much exposure, and is far-removed from attainable, real-world results. Further, the model appears to provide little opportunity for diversification, which will make retained earnings growth that much more difficult to realize. **It is apparent from these assumptions that NCUA is attempting to eliminate risk at the corporate level, as opposed to permitting corporate credit unions to manage risk. Such a business model is unreasonable and counterproductive and, ultimately, will be crippling to the corporate network.** We believe such a "managing down" of corporate balance sheets to the natural person credit union tier would introduce greater instability, risk, burden, and costs into the credit union system, and would pose ever greater risk and losses to the NCUSIF. This consequence of NCUA's retained earnings growth model proposed is alarming and a further indication of the impractical and non-synchronous nature of the proposal. Given the severe risks posed to natural person credit unions and the share insurance fund, we recommend that NCUA consider the unintended consequences of pushing the investment function down to natural person credit unions that, for the most part, lack adequate expertise to safely manage investment portfolios.

We are aware that NCUA has made public statements indicating that it will announce plans by April 2010 for addressing legacy assets. We are baffled as to why this critical topic is not mentioned at all in the proposed rule. Dealing with investment securities remaining on corporates' books is vital to realizing any lasting, consequential changes to the corporate system. We believe that failure to address this issue invites the weakening of even currently stable corporates, and would serve to negate the positive changes that NCUA and credit unions would like to see in the corporate system. **We strongly urge NCUA to cooperatively and transparently address the business and regulatory issues associated with these assets so that corporate credit union balance sheets can start with a "clean slate," rather than from a negative position.** We would like to point out that, in addition to the proto-typical assets on corporate balance sheets, NCUA should also address any problem assets that may reside on the balance sheets of corporate credit union service organizations.

The proposal requires, as qualification for directorship, that all candidates must currently hold the equivalent of a CEO, CFO, or chief operating officer (COO) position at the member institution (typically, though not always, a natural person credit union). We do not agree that a particular job title necessarily makes for a better board member, and instead suggest that NCUA consider that directors of corporates that may not have full experience or training needed in a particular area be required to obtain training on an annual or other periodic basis as a condition of service on a corporate board. **In case it's been overlooked, most if not all of the Board members of the conserved corporates bore these titles.** We clearly disagree with the proposed six year term limit for corporate directors, and instead propose that this be changed to a nine year limit. Further, we believe that outside directors with investment expertise should be permitted to serve, as long as adequate safeguards are in place to address conflicts of interest between an outside director's professional investment interests and his/her responsibility to preserve the confidential and proprietary interests of a corporate credit union.

We believe that corporate consolidation would be beneficial to the system, and that NCUA should be more open, responsive, and supportive of such consolidation by removing unreasonable impediments and/or resistance to corporate credit union mergers. We recognize that the current number of corporates is less than ideal with respect to efficiency and effectiveness (e.g., potentially redundant member capital requirements, duplication of expertise, staffing, and infrastructure). **Why not allow the market place to choose, and not over-zealous regulation!**

Ultimately, 90 million credit union members rely on the corporate system to provide trading, payments, clearing, and settlement services for their local credit unions. Given this systemically important role that the corporate credit union network plays in our nation's "financial system," it would appear that preservation of a corporate credit union option is tantamount to preserving the credit union option, locally, for everyday consumers in our country.

There is no question that the NCUA put a great amount of effort and thought into this proposed regulation; however, it is not viable in its current form, nor does it appear to be fair and balanced in its approach. **If it is permitted to be enacted as drafted, it will make it virtually impossible for corporate credit unions to operate in any kind of viable manner.**

We urge the Board to strike an effective and fair balance between preventing a repeat of past corporate failures and allowing a viable corporate system to thrive. **We again ask NCUA to withdraw this proposal and consider another round of proposed rule-making with a 90-day comment period by the credit union system before issuing final rules.** The gravity of possibly losing the corporate credit union system as an option for natural person credit unions justifies a comprehensive "reality check" on what NCUA has proposed for the future of corporate credit unions and, ultimately, natural person credit unions.

I'm sure the comments contained herein have rendered themselves to too much detail, and yet I hark back to my opening remarks, and that is the context and paradigm which I am coming from. There is something inherently good and valuable about history and living through the historical experiences, especially within the financial world. As a credit union that had $100,000 in Penn Square Bank, and whose CEO went to Texas and literally stood in line to capture those funds from the FDIC, it has left an indelible impression upon my life and my management to hopefully never expose this credit union nor the credit union system that I truly love and value to such risk that now could occur once again. As I've stated, I do respect the well placed intentions to limit risk, but I believe the authors of the proposed regulation simply don't have the context to fully understand that if the corporate credit union system is abandoned that credit unions will have severe challenges in the years to come in the most important areas of liquidity, investment s, lines of credit, and payment and check clearing processing. In asking for an extension of time, I trust this will provide a more collaborative effort to take into account some of the historic lessons that unfortunately we have learned that I trust we will never have to repeat and provide us with an efficient, productive and state of the art corporate credit union system that all of America's credit unions and our over 90 million members need.

Sincerely,

Mendell L. Thompson

Cc: Board of Directors
Supervisory Committee
Terri Snyder, SVP/COO
Nicki Harms, CFO